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China - Peoples Republic of

Cotton and Products Update

Imports of U.S. Cotton Rebound as Total Cotton Imports Recover

Approved By:

Michael Ward

Prepared By:

Jennifer Clever

Report Highlights:

Post's forecast for MY17/18 domestic cotton production is raised to 5.4 MMT, up 9 percent from the previous year. Higher cotton prices in MY16/17 and continued government support to cotton production stimulated acreage recovery. Favorable weather conditions also contributed to higher yield in MY17/18. China's cotton use is expected to recover to 8.5 MMT in MY17/18 mainly due to the narrowing gap between domestic and global cotton prices. Yarn imports are expected to fall as domestic yarn made from cotton stocks becomes more price-competitive. Correspondingly, MY17/18 ending stocks are forecast to decline to 8.73 MMT with stocks to use ratio falling to 103 percent. Given the Chinese textile sector's increasing demand for high-grade cotton, traders anticipate the government may increase its flexibility in issuing additional import quotas. Hence, China's cotton imports are expected to increase to 1.3 MMT in MY17/18 from the 1.1 MMT in MY16/17. After falling to their lowest level in 14 years, China's imports of U.S.

cotton rebounded in MY16/17 and are likely to exceed 500,000 tons in MY17/18.

Executive Summary:

Post's forecast for MY17/18 domestic cotton production is raised to 5.4 MMT, up 9 percent from the previous year. Higher cotton prices in MY16/17 and continued government support to cotton production stimulated acreage recovery. Favorable weather conditions also contributed to higher yield in MY17/18. China's cotton use is expected to recover to 8.5 MMT in MY17/18 mainly due to the narrowing gap between domestic and global cotton prices. Yarn imports are expected to fall as domestic yarn made from cotton stocks becomes more price-competitive. Correspondingly, MY17/18 ending stocks are forecast to decline to 8.73 MMT with stocks to use ratio falling to 103 percent. Given the Chinese textile sector's increasing demand for high-grade cotton, traders anticipate the government may increase its flexibility in issuing additional import quotas. Hence, China's cotton imports are expected to increase to 1.3 MMT in MY17/18 from the 1.1 MMT in MY16/17. After falling to their lowest level in 14 years in MY15/16 to 192,000 tons, Chinese imports of U.S. cotton rebounded to 501,000 tons in MY16/17. China's imports of U.S. cotton are likely to exceed 500,000 tons in MY17/18.

China's MY17/18 Cotton Production is Expected to Recover to 5.4 MMT

Post's forecast for MY17/18 domestic cotton production is 5.4 MMT, up 9 percent from an estimated 4.95 MMT in MY16/17. The forecast recovery is based on a 5.9 percent expansion in planted area to 3.12 MHa, and on higher yield. Increase in cotton prices and profits during MY16/17, and the government's continued subsidies to Xinjiang province contributed to the cotton area expansion (see GAIN report CH17014), while favorable weather conditions contributed to higher yield in MY17/18.

Based on an October survey, the China Cotton Association (CCA) forecast for MY17/18 cotton production is 5.5 MMT, up 11.5 percent from MY16/17 and slightly lower than its previous estimate of 5.54 MMT. Specifically by region, Xinjiang production is 4.43 MMT, up 12.3 percent over the previous year. Comparatively, forecast MY17/18 combined production for the Yangtze River and the Yellow River regions stands at 1 MMT, up 7.7 percent over the previous year, unchanged from CCA's previous forecast. Despite the slight recovery of cotton acreage in the Yangtze River and Yellow River regions in MY17/18, the cotton production gain in these regions does not contribute significantly to the nation's overall cotton production.

The CCA survey also showed that generally favorable weather conditions in October facilitated the cotton harvest nationwide. However, excessive rain in the west region of the Yellow River and part of the Anhui and Hubei lowered cotton quality. As of the end of October, cotton harvest was 83.6 percent completed and 9.8 percentage points higher than the previous year. The marketing of seed cotton was also 12 percentage points faster than the previous year. Specifically, harvest in North Xinjiang ended, while in South Xinjiang continues and is expected to finish by the end of November, two weeks later than the previous year. The average price for seed cotton is down 6.2 percent from the previous year. Additionally, MY17/18 cotton quality improved greatly in Xinjiang. In particular, 80 percent of the cotton produced in North Xinjiang showed both length exceeding 28 mm and breaking strength exceeding 28 grams/tex.

MY17/18 Cotton Harvest and Marketing Pace

	Harvest Completed%	Change *	Seed Cotton Marketing Rate%	Change *
Nation Average	83.6	9.8	65.7	12
Northwest(Xinjiang and Gansu)	83.7	12	97.5	13.5
The Yellow River Region	92.2	0.6	18.8	-4.2
The Yangtze River Region	71	1.3	28.9	3.6

Source: As of the end of October, 2017 by CCA; * percentage points as compared to the previous year

The Chinese Ministry of Agriculture (MOA)'s November forecast for MY17/18 cotton production is 5.32 MMT, up 10.4 percent from MY16/17. The higher cotton production is a combination of a 6.2 percent acreage expansion and a 3.9 percent gain in yield compared to MY16/17. Based on its October survey data, another leading industry source also echoed a higher cotton production for MY17/18 at 5.4 MMT, up 15 percent from its estimated 4.69 MMT for MY16/17.

As of November 26, 2017, total classified MY17/18 cotton stood at 2.88 MMT, of which Xinjiang accounts for 97.9 percent at 2.82 MMT. The high rate of cotton classification in Xinjiang is related to the government's subsidy policy (official classification is a prerequisite for entitlement of the subsidy). The low volume classified in all none-Xinjiang regions reflects a low production coupled with a liberalized ginning market, and lower incentive for official classification.

Cotton Production Estimate/Forecast by Various Sources (MMT; MHa)

	CCA	MOA	NSB	Post
MY15/16 Acreage/Production	3.21/ 4.82	3.27/ 4.93	3.8/ 5.6	3.05/ 4.8
MY16/17 Acreage/Production	2.75/ 4.94	3.1/ 4.82	3.38/ 5.34	2.95/ 4.95
MY17/18 Forecast acreage/production	2.83/ 5.5	3.29/ 5.32	NA	3.12/ 5.4
MY17/18 production change	+11.5%	+15.0%	NA	+9.0%

CCA- China Cotton Association; MOA-China's Ministry of Agriculture; NSB – National Statistics Bureau

Stocks

Post's forecast for China's cotton stocks remain high at 8.73 MMT by the end of MY17/18. However, this level is significantly lower than the 10.5 MMT at the end of MY16/17. Increased use of state reserves and the moderate recovery in cotton consumption accounted for the reduction in stocks. In addition, expected limited cotton imports, as a direct result of restrictions on additional import quotas, will also contribute to ending stocks falling in MY17/18.

Based on the National Development and Reform Commission (NDRC)'s notice dated November 9, 2017, sales of State Cotton Reserves for 2018 are scheduled to start on March 12 and end at the end of August 2018. Similar to previous years, the daily volume for auction will be about 30,000 tons. In case of constant price increase in both domestic and international markets and the daily purchase rate exceeding 70 percent for 3 days in a week, the daily auction volume will be adjusted to increase

accordingly. The basic auction price formulation will likely continue (more market-oriented, not fixed) and based on the average between the domestic and international spot market cotton price indexes during the previous week. If necessary, the government can consider other measures, including extending the time for sales, to meet the market demand for cotton.

The 2017 government cotton reserve sales began on March 6 and ended at the end of September with 3.22 MMT of state reserve sold to the industry. The previous announcement of the 2018 sales plan indicates that the government's priority for 2018 remains focused on reducing state reserves to a “reasonable level” while assuring the spinning sector utilizes the state cotton reserves as its main source for cotton. However, this will not ease the shortage of high grade cotton for Chinese mills. Industry sources estimate that the current government cotton reserve stands at about 5.2 MMT. If another 3 MMT of state cotton reserve can be used in 2018, the state cotton reserve could fall to a more manageable level compared to the 13.9 MMT in MY14/15, when China’s cotton reserves peaked after three years of state supported purchase programs. ([See GAIN Report CH15011](#))

MY17/18 Cotton Consumption Expected to Grow to 8.5 MMT

MY17/18 cotton consumption is forecast at 8.5 MMT, up from an estimated 8.16 MMT in MY16/17. The growth in cotton use is mainly driven by a more market-oriented domestic cotton price. This price is expected to reduce yarn imports and stimulate cotton fiber use in yarn production. Anticipated growth in domestic demand for textiles and apparel is also expected to moderately boost China’s cotton consumption. Meanwhile, facing stronger global competition, Chinese exports of textile and apparel are expected to remain stable with no significant increases.

Forecast lower yarn imports will stimulate China’s cotton consumption. In previous years, increased yarn imports significantly reduced China’s cotton use for spinning. The average net yarn imports hit 1.8 MMT per year from MY14/15 to MY15/16 compared to 0.5 MMT per year from MY09/10 to MY10/11. Industry sources indicate that the shrinking gap between the domestic and international cotton prices will encourage more domestic spinning. Cotton utilization in yarn production is expected to continue recovering in MY17/18 in response to a more market-oriented cotton price.

According to the China Textile Association, China’s textile sector grew steadily in the first eight months of 2017, with total output value up 8.3 percent and total profits up 10.3 percent compared to the previous year. Preliminary statistics show that in the first ten months of 2017 total production of yarn increased by 4.34 percent, fabrics by 2.32 percent, and apparel by 1.9 percent, respectively.

China’s Yarn and Fabrics Production in 2017 (Jan-Oct)

	Production	Change YOY
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Total Yarn (1,000 tons)	35,200	4.34%
--Cotton Yarn	24,029	3.38%
--Cotton Blended Yarn	5,450	7.41%
Total Fabrics (million meters)	58,815	2.32%
--Cotton Fabrics	32,204	2.12%
--Cotton Blended Fabrics	11,944	5.08%

Source: China Cotton Textile Association

It is worth noting that in 2016, textile investment in Xinjiang soared to RMB48 billion (\$7 billion) from RMB9.6 billion (\$1.4 billion) in 2014. Total spindles are expected to more than double to 16 million by the end of 2017 compared to 7 million in 2014. Total yarn production is likely to reach 1.5 MMT in 2017, consuming 1.4 MMT of cotton or roughly one third of Xinjiang's cotton production. By comparison, in 2016, total yarn production was 1.13 MMT and cotton use was about 1 MMT. Xinjiang's favorable policies, including tax reductions, and favorable electricity prices will continue to attract more investment in the textile and apparel industry in 2018 and beyond.

Currently, in response to the domestic shortage of high-grade cotton, many mills use machine harvested cotton produced by Xinjiang Production and Construction Corp (PCC), whose quality is reported to be much better than last year. However, imported high count yarn remains more competitive to domestic yarn given the higher price for high-grade cotton in the domestic market. Currently, mills in east China have switched to producing more blended yarn to stay competitive while Xinjiang mills produce more pure cotton yarn.

Exports of textiles and apparel expected to stabilize

Chinese Customs' data shows that during the first ten months of 2017, total Chinese textile and apparel exports stood at \$221.47 billion, slightly down from the previous year. Out of this total, exports of textile products were up 2.5 percent and valued at \$90.34 billion while the value of apparel exports declined by 2.45 percent. Total textile and apparel exports in October grew steadily with export value up more than 1 percent over the previous year. Given the more competitive domestic cotton price, Chinese industry experts remain optimistic about the prospects for stable exports in 2018.

Growth in domestic demand for textile and apparel drives cotton use

China's overall increase in demand for textile and apparel products is fueled by higher disposable income, rising living standards, population growth, and urbanization. During the first three quarters of 2017, China's economic growth (GDP) reached 6.9 percent. Chinese policy allowing a second child per couple contributed to about 1.3 million more new births in 2016 compared to the previous year. According to Chinese industry statistics, in the first eight months of 2017, the total domestic sales value of apparel and other textile products increased 7.3 percent and online shopping for clothing increased by 19.6 percent from the previous year. These indicators suggest a steady recovery of the Chinese textile industry and support greater cotton use in MY17/18.

Cotton Trade

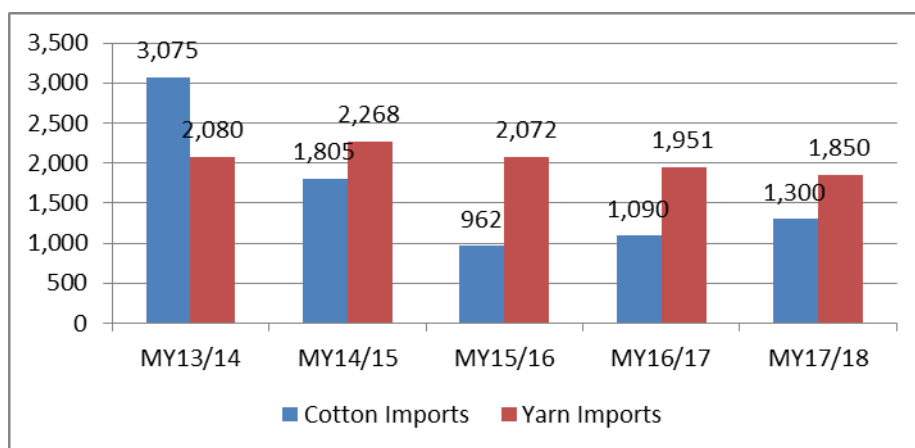
Cotton imports expected to grow to 1.3 MMT in MY17/18

MY17/18 cotton imports are forecast to recover to 1.3 MMT from MY16/17 at 1.09 MMT based on a forecast recovery in high-grade cotton consumption and a decline in yarn imports in 2018. The Chinese textile industry's demand for higher-grade cotton is primarily satisfied by imports. However, the government's restriction on additional quota imports, subject to a sliding duty and outside the tariff rate quota amount committed under the World Trade Organization (WTO), have tempered the prospects for any significant increases in cotton imports. The WTO quota allows a yearly volume of 894,000 tons subject to a one percent import tariff. The Chinese government has suspended the distribution of additional quotas since 2016.

Since July 2017, anecdotal reports have circulated that the government might be considering special approval to allow for some imports of high-grade cotton. As of the date of this report, there have been no official announcements in this regard. A relatively large Xinjiang crop of "higher" grade cotton could partially meet the industry demand in MY17/18. Liberalized yarn imports can also alleviate the shortage of high count yarn for fabric manufacturing. The Chinese textile sector grew steadily in 2017. In consideration of all these factors, it is logical for the government to approve some cotton imports to meet the industry demand in 2018.

In late November 2017, the China Cotton Textile Association (CCTA) held a Cotton Textile Conference in Shanghai attended by representatives of the National Development and Reform Commission (NDRC) and other relevant government agencies. At the conference, Chinese industry advocated that the government add more import quotas to meet industry demands for imported cotton and bring more balance to the domestic cotton market. It was also suggested that the sales of state reserves be conducted beyond the March-August window to all year around. Lastly, the industry also recommended that China develop a plan to improve the quality mix of the state reserves by importing cotton when the price gap between the domestic and international markets exceed 1500RMB/ton. Conference participants argued that such a plan would enhance the government's ability to regulate China's cotton market. It remains unclear when the government will allow additional cotton imports. Given the government's traditional role in regulating the cotton market, any form of intervention should be expected.

Cotton Imports vs Yarn Imports (MY13/14 to MY17/18; in 1,000 tons)



Source: Global Trade Atlas (MY16/17 estimate and MY17/18 forecast by FAS/Beijing)

In recent years, yarn imports have been an important factor exerting downward pressure on cotton imports. Unlike cotton imports, yarn imports do not face quota restrictions and enjoy a low import duty. Higher imports of yarn partially lowered cotton imports in 2015 and 2016. In MY16/17, total yarn imports from China's top three supplying countries (namely Vietnam, India and Pakistan) accounted for 72.6 percent. Of note, yarn imports from Vietnam have grown rapidly in the last three years as many mills have moved from China to Vietnam. This trend is expected to continue mainly as Vietnam does not maintain quotas on cotton imports and Vietnamese yarn exports to China enjoy a zero duty.

China's Yarn Imports by Major Suppliers (1,000 tons)

	MY14/15	MY15/16	MY16/17	MY16/17 Share	Import Tariff Rate
World	2,268	2,072	1,951		
Vietnam	481	552	687	35.2%	0
India	631	557	379	19.4%	3.5%
Pakistan	568	422	351	18.0%	3.5%

Source: Global Trade Atlas

The smaller gap between domestic and international cotton prices reduced the profitability of yarn imports and has lowered yarn imports since April 2017. Industry sources report that yarn imports are expected to tentatively rebound during the last two months of 2017 in response to a larger gap between domestic and imported yarn prices. In general, yarn imports are forecast to decline moderately which may facilitate cotton imports in MY17/18.

Chinese Imports of U.S. cotton rebound but U.S. cotton still faces competition from other suppliers

After falling to their lowest level in 14 years in MY15/16 to 192,000 tons, Chinese imports of U.S. cotton rebounded to 501,000 tons in MY16/17. This accounts for 46 percent of China's total cotton imports in MY16/17. Although the quality and reliability of U.S. cotton appeals to China's end-

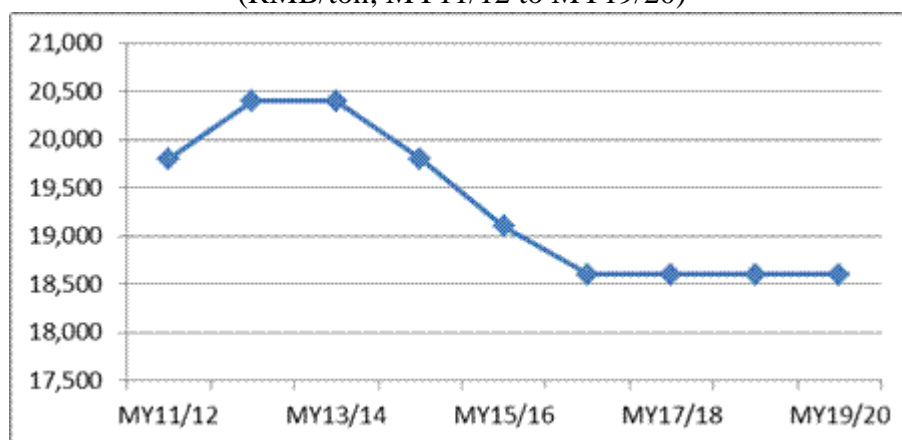
users, in MY15/16, Australian cotton became very competitive and topped China's market with 268,000 tons. Given Chinese buyers' preference for high-grade cotton when import quotas are limited, Chinese imports of U.S. cotton are likely to exceed 500,000 tons in MY17/18.

Chinese cotton exports remains insignificant

China's cotton exports stand at 13,000 tons in MY16/17, down from 28,000 tons during the previous year. Given the relatively low quality at a high price, sporadic exports of Chinese cotton are likely to continue in 2018 and beyond but are expected to remain insignificant.

Policy

China Cotton Support Policy Evolution
(RMB/ton; MY11/12 to MY19/20)



Note: MY11/12 to MY13/14 is government purchase floor price;
MY14/15 to MY19/20 is “target price” for Xinjiang only; Source: NDRC

The fixed “Target Price” (at RMB18,600 or \$2,776/ton) for Xinjiang from 2017 to 2019 is expected to stabilize cotton acreage in Xinjiang. The MY17/18 implementation of the target price-based subsidy in Xinjiang is expected to stay unchanged from MY16/17. In general, Xinjiang farmers welcome this policy as it provides predictability and assures the basic farming profits.

As of this report, there is no official announcement for the fixed subsidy (RMB2,000 or \$313/ton) for the other nine cotton-producing provinces. In consideration of the reduction in cotton planting in these provinces and the shortage of domestic cotton supply and use in the post “high state reserves” era, China's industry leaders continue to call for the central government to maintain similar support to these provinces as it does for Xinjiang. To prevent further reductions in cotton acreage in these provinces, Provincial governments are taking their own steps to stabilize local production. In Hebei Province for example, the provincial government has designated 200,000 Ha of land as a “cotton protection area.”

Tables

Production, Supply and Demand (PSD)

Table 1. PSD (in 1,000 Bales and 1,000 Ha)

Cotton China	2015/2016		2016/2017		2017/2018	
	Market Year Begin: Aug 2015		Market Year Begin: Aug 2016		Market Year Begin: Aug 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Planted	0	3,050	0	2,950	0	3,125
Area Harvested	3,050	3,050	2,900	2,950	3,125	3,125
Beginning Stocks	66,920	66,920	58,198	58,198	48,419	48,419
Production	22,000	22,000	22,750	22,750	25,000	24,800
Imports	4,406	4,406	5,032	5,032	5,300	5,971
MY Imports from U.S.	0	880	0	2,302	0	2,985
Total Supply	93,326	93,326	85,980	85,980	78,719	79,190
Exports	128	128	61	61	50	60
Use	35,000	35,000	37,500	37,500	39,000	39,040
Loss	0	0	0	0	0	0
Total Dom. Cons.	35,000	35,000	37,500	37,500	39,000	39,040
Ending Stocks	58,198	58,198	48,419	48,419	39,669	40,090
Total Distribution	93,326	93,326	85,980	85,980	78,719	79,190
Stock to Use %	166	166	129	129	102	103
Yield	1,570	1,570	1,708	1,679	1,742	1,728
TS=TD	0	0	0	0	0	0

Table 2. PSD (in 1,000 Tons and 1,000 Ha)

Cotton China	2015/2016		2016/2017		2017/2018	
	Market Year Begin: Aug 2015		Market Year Begin: Aug 2016		Market Year Begin: Aug 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Planted	0	3,050	0	2,950	0	3,125
Area Harvested	3,050	3,050	2,900	2,950	3,125	3,125
Beginning Stocks	14,570	14,570	12,671	12,671	10,542	10,542
Production	4,790	4,790	4,953	4,953	5,443	5,400
Imports	959	959	1,096	1,096	1,154	1,300
MY Imports from U.S.	0	192	0	501	0	650
Total Supply	20,319	20,319	18,720	18,720	17,139	17,241
Exports	28	28	13	13	11	13
Use	7,620	7,620	8,165	8,165	8,491	8,500
Loss	0	0	0	0	0	0
Total Dom. Cons.	7,620	7,620	8,165	8,165	8,491	8,500
Ending Stocks	12,671	12,671	10,542	10,542	8,637	8,728
Total Distribution	20,319	20,319	18,720	18,720	17,139	17,241
Stock to Use %	166	166	129	129	102	103
Yield	1,570	1,570	1,708	1,679	1,742	1,728
TS=TD	0	0	0	0	0	0

